Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of	)	
	)	
Petition of BellSouth Telecommunications,	)	WC Docket No. 05-342
Inc. For Forbearance Under 47 U.S.C. § 160	)	
From Enforcement of Certain of the	)	
Commission's Cost Assignment Rules	)	

Reply Comments of the
Ad Hoc Telecommunications Users Committee

The Ad Hoc Telecommunications Users Committee ("Ad Hoc") hereby submits its Reply to comments filed in support of BellSouth's petition seeking forbearance from enforcement of Commission cost assignment rules.

The New Jersey Division of the Ratepayer Advocate (New Jersey) and Time Warner Telecom (TWT) also filed comments opposing BellSouth's Petition. Ad Hoc will not use this Reply to repeat the positions and reasoning set forth in those petitions. Suffice it to say that the New Jersey and TWT oppositions alone, and in conjunction with Ad Hoc's Opposition, require denial of BellSouth's petition.

Although AT&T and Verizon urge the Commission to grant BellSouth's petition, they offer nothing new in support. Indeed, Verizon uses its comments to argue principally for extension of the current Separations freeze and for Commission confirmation that the Separations freeze precludes states from imposing inconsistent Separations requirements.

AT&T, on the other hand, attempts, albeit unsuccessfully, a broader based support for BellSouth's petition. AT&T argues that cost allocation and assignment rules have no applicability under the Commission's price cap system;[1] that costs are not used to ensure just and reasonable rates;[2] and that price cap rules prevent carriers from imposing rates that are unjust and unreasonable.[3] AT&T's arguments simply are without merit.

I. Reliable Cost Data Must Remain Available Under Price Caps Regulation.

Ad Hoc's opposition demonstrated that the Commission's price caps rules do not sever the relationship between rates and costs. Ad Hoc explained that cost and revenue data are important under price caps regulation because the data allow calculation of earnings, which are important to assessing the efficacy of the currently effective price caps regulatory mechanism.[4] Contrary to AT&T's contention, no inherent feature of price caps regulation assures just and reasonable rates. Price caps regulation is intended to encourage more efficient carrier behavior and produce results that are closer to those that a competitive market would yield. In effectively competitive markets, marketplace forces drive prices to levels that yield fair returns given the relevant degree of risk. However, in the absence of effective competition, regulatory intervention is warranted. The Commission's current form of rate regulation is "price caps." Under price caps, or any form of rate regulation, the Commission should periodically assess

[1] AT&T, Comments at 3.
[2] *Id.* at 4.
[3] *Id.*
[4] Ad Hoc, Comments at 14-15.

whether its regulatory model has produced a competitive result, *i.e.*, whether the returns realized by price caps carriers are just and reasonable under section 201 of the Communications Act of 1934, as amended. As Ad Hoc noted in its comments, "Carrier earnings that consistently were too low or too high would suggest revisions to the formulae."[5] Without the cost allocation and assignment rules BellSouth and other price caps carriers could manipulate earnings data and certainly camouflage excessive earnings, and thus hide the need for adjustments to the price caps formulae. The price caps formulae might need substantial adjustment, but the Commission would not know that. Consumers would be subject to price gouging, but the Commission would know that price gouging was happening. Surely the Commission will not allow that to happen. Allowing such conditions to pertain would amount to rate deregulation without a record to support deregulation.

Ad Hoc's comments also explained that cost data is relevant to requests to price above and below established pricing bands and to applications to recognize exogenous cost changes under section 64.45(d) of the Commission's rules.[6] Ad Hoc also reminded the Commission that the so-called CALLS plan has expired and may be replaced with a form of price caps regulation that uses a productivity offset to establish price cap indices and that cost data are needed to set the productivity offset at a proper level.[7] Thus, the Commission must reject

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5 *Id.*
6 *Id.* at 15-16.
7 *Id.*

as without merit assertions by BellSouth and its supporters that cost data are irrelevant to price caps regulation.

II. Market Places Forces Are Insufficient To Justify Forbearance.

Assertions by BellSouth and AT&T that competition eliminates any need for rate regulation and thus any need for relevant cost data are also meritless. Market forces are insufficient to control BellSouth's pricing of special access services. The Commission need only review the record in the Special Access rate investigation to confirm this conclusion.[8] Ad Hoc's comments reminded the Commission that BellSouth's special access return is so high (in excess of 80% in 2004) that it belies any assertion that the special access market is effectively competitive.[9] Service providers do not realize such a return when a market is competitive.

Not just the special access market lacks effective competition, terminating switched access also is not provided in a competitive market. When a long distance call is terminated, or a toll free call is initiated, the long distance carrier who must pay for access service, does not select the provider of terminating access. Instead terminating access is provided by a carrier selected by an end user who may, of course, use a long distance carrier other than the long distance carrier terminating traffic. The long distance carriers cannot use market alternatives to control their terminating access service costs. In short there is

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[8] *Special Access Rates for Price Cap Local Exchange Carriers,* WC Docket No. 05-25, *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services,* RM-10593, Order and Notice of Proposed Rulemaking, FCC 05-18 (rel. January 31, 2005).

[9] Ad Hoc, Comments at 6-7.

market failure.[10] Because of this market failure, the Commission has concluded that it cannot take a hands-off approach with respect to terminating access. If the Commission were, however, to grant BellSouth's petition, it would, in effect and without justification, reverse itself by effectively deregulating interstate terminating access service rates.

Nor can the Commission logically conclude that effective competition exists with respect to originating access service. Initially the Commission exercised no regulation of access service rates imposed by competitive local exchange carriers (CLECs) believing that the rates charged by incumbent access service carriers would restrain CLEC access service rates.[11] In the Seventh and Eighth Reports and Orders in the *Access Charge Reform* proceeding, the Commission addressed disputes between long distance carriers and CLECs over the CLECs' access service rates.[12] The Commission in effect concluded that the competition that may exist for consumer access lines does not equate to competition for access service. In the *Seventh Report and Order* at 9935 (para. 31)*,* the Commission explained that,

> [A]lthough the end user chooses her access provider, she does not pay that provider's access charges. Rather, the access charges are paid by the caller's IXC [long distance service provider], which has little practical means of affecting the caller's choice of

[10] *See, Access Charge Reform,* CC Docket No. 96-262, First Report and Order, 12 FCC Rcd 15982, 16135-36 (19997), *aff'd sub. Nom., Southwestern Bell v. FCC,* 153 F.3d 523 (8th Cir. 1998).

[11] Of course, the Commission has always regulated the interstate access service rates charges by dominant providers of exchange access service.

[12] *Access Charge Reform,* CC Docket No. 96-262, Seventh Report and Order, 16 FCC Rcd 9923 (2001); *Access Charge Reform,* CC Docket No. 96-262, Eighth Report and Order, 19 FCC Rcd 9108 (2004).

> access provider (and even less opportunity to affect the called party's choice of provider) and thus cannot easily avoid the expensive ones. Second, the Commission has interpreted section 254(g) to require IXCs geographically to average their rates and thereby to spread the cost of both originating and terminating access over all their end users. Consequently, IXCs have little or no ability to create incentives for their customers to choose CLECs with low access charges. Since the IXCs are effectively unable either to pass through access charges to their end users or to create other incentives for end users to choose LECs with low access rates, the party causing the costs – the end user that chooses the high-priced LEC – has no incentive to minimize cost.

The Commission's own analysis shows that the market cannot provide a check on LEC pricing for access service. Accordingly, it is little wonder that to date the Commission has not even suggested deregulating switched access charges. But deregulation is effectively the relief sought by BellSouth, because without reliable cost data, price caps regulation has extremely limited utility as a mechanism to regulate the access service rates charged by price cap carriers. Is the Commission willing to accept the consequences of effectively deregulating interstate access charges? Ad Hoc thinks not, and accordingly, submits that the market failure dynamic that is inherent in the access service market is another reason to deny BellSouth's petition.

The Commission should also consider whether it is willing to lose access to important cost data that will be relevant to general reform of inter-carrier carrier compensation mechanisms. There is no rational basis for assuming that price caps local exchange carriers should be allowed to recover the same revenues under a reformed inter-carrier compensation mechanism as they currently realize. At the very least, that should be an open issue that the Commission should not now prejudge. But prejudge the issue it will, if it were to grant BellSouth's petition.

III. Conclusion

In view of the foregoing, Ad Hoc urges the Commission to deny the above-captioned petition for forbearance.

Respectfully submitted,

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